

executed, the amount realised by the execution by the Collector has to be taken into account. When the Subordinate Judge, Purnea, has to decide the question whether the application for execution made to him is in continuance of an existing execution proceeding, he has to recognise the proceeding before the Additional Collector, Banares, as a proceeding in execution under the Code for it is so under the Act. In doing this, for the reasons earlier mentioned, he would not be giving any extra-territorial operation to the Act. It seems to us therefore that the execution of the decree by the Collector must be deemed to be execution of a decree for all purposes and therefore an application made to the Subordinate Judge, Purnea, for execution of the same decree while an execution proceeding was pending before the Collector, must be a continuation of the execution last mentioned. No question of limitation can arise in regard to such an application.

1959
Additional
Collector, Banares
v.
Maharaj
Kishore Khanna
Sarkar J.

We think therefore that this appeal must succeed. We set aside the order of the High Court and restore the order of the Subordinate Judge, Purnea. The respondent will pay the costs of the appellant in this Court and in the High Court.

Appeal allowed.

THE COMMISSIONER OF INCOME-TAX,
HYDERABAD-DECCAN

1959
March 20.

v.

MESSRS. VAZIR SULTAN & SONS

(N. H. BHAGWATI, B. P. SINHA and
J. L. KAPUR, JJ.)

Income Tax—Capital or income—Compensation for termination of agency—Agency terminable at will—Partial termination of agency—Sterilisation of asset or loss of profit—Indian Income-tax Act, 1922 (XI of 1922).

In 1931 the respondent, a registered firm, was appointed the sole selling agents and distributors for the Hyderabad State of

1959

The Commissioner
of Income-tax,
Hyderabad-Deccan

v.

Messrs. Vazir
Sultan & Sons

cigarettes manufactured by V (a limited company) under the terms of a resolution of the Board of Directors, the agency commission being a discount of 2% on the gross selling price. In 1939 another arrangement was made whereby the respondent's agency was extended to the rest of India. By a resolution dated June 16, 1950, the agency of 1939 was terminated on payment of Rs. 2,26,263 to the respondent by way of compensation, but the respondent continued to be distributors for the Hyderabad State. For the assessment year 1951-52 the Income-tax Officer included the aforesaid sum in the respondent's total income and taxed it as a revenue receipt under the head of "business". The respondent claimed that it did not carry on business of acquiring and working agencies, that the agency acquired in 1931 was a capital asset of its business of distributing cigarettes in the Hyderabad State, that the expansion of territory outside the Hyderabad State in 1939 was an accretion to the capital asset already acquired by it, that the resolution of 1950 was in substance a termination of the agency qua territory outside the Hyderabad State which resulted in the sterilisation of the capital asset qua that territory, that the sum of Rs. 2,19,343 received by it in the year of account was by way of compensation for the termination of the agency outside Hyderabad State and being therefore compensation for the sterilisation *pro tanto* of a capital asset of its business was a capital receipt and therefore was not liable to tax. It was contended on behalf of the Income-tax Authorities that the sole selling agency which was granted by the company to the assessee in the year 1931 was merely expanded as regards territory in 1939 and what was done in 1950 was to revert to the old arrangement, that the structure or the profit-making apparatus of assessee's business was not affected thereby, that the expansion as well as the restriction of the assessee's territory were in the ordinary course of the assessee's business and were mere accidents of the business which the assessee carried on and that the sum of Rs. 2,19,343 received by the assessee as and by way of compensation for the restriction of the territory was a trading or an income receipt and was therefore liable to tax. It was also urged that the agency agreement between the respondent and the company was terminable at the will of the latter and so it could not be considered as an enduring asset.

Held (per Bhagwati and Sinha, JJ., Kapur, J., dissenting) that the agency agreements in question did not constitute the business of the respondent, but formed a capital asset, being the profit-making apparatus of its business of distribution of the cigarettes manufactured by the company within the respective territories, and, consequently, any payment made by the company as compensation for terminating the agency would only be a capital receipt in the hands of the respondent.

Commissioner of Income-tax v. Shaw Wallace & Co., (1932)
L. R. 59 I. A. 206, relied on.

Commissioner of Income Tax and Excess Profits Tax, Madras v. The South India Pictures Ltd., Karaikudi, [1956] S.C.R. 223 and *Commissioner of Income-tax, Nagpur v. Rai Bahadur Jairam Valji*, [1959] Supp. 1 S.C.R. 110, distinguished.

Case law reviewed.

Held, further, that the fact that the agency agreements were terminable at will, or that only one of them was terminated, would not make any difference because in either case, when the agency was terminated and the amount was paid as compensation for such termination it resulted in the sterilisation of the capital asset *pro tanto* and it was received as a capital receipt in the hands of the respondent.

Glenboig Union Fire-Clay Co., Ltd. v. The Commissioners of Inland Revenue, (1922) 12 Tax Cas. 427, relied on.

Per Kapur, J.—The true effect of the facts of the present case was that in 1939 the respondent's area of distribution was increased from the State of Hyderabad to the whole of India and in 1950 it was again reduced to the original area of 1931, so that the respondent did not lose its agency. Consequently, the termination of the agency in 1950 did not affect the trading activities of the respondent and, therefore, viewed against the background of the respondent's business organisation and profit-making structure the compensation for the termination of the agency was no more than that for the loss of future profit and commission. The compensation therefore was in the nature of surrogatum and in this view of the matter it was revenue and not capital.

The answer to the question, as applied to agencies, whether the compensation is capital or revenue, is that it will be a capital receipt if it is received as the value of the agency, i. e., it is a price of the business as if it is brought to sale. On the other hand it is revenue receipt if it is paid in lieu of profits or commission.

In view of the decision *The Commissioner of Income-tax v. The South India Pictures Ltd., Karaikudi*, [1956] S.C.R. 223, and the observations of Bose, J., in the case of *Raghuvanshi Mills Ltd. v. Commissioner of Income-tax*, [1953] S.C.R. 177, the authority of *Commissioner of Income-tax v. Shaw Wallace & Co.*, (1932) L.R. 59 I.A. 206, must be taken to be considerably shaken.

CIVIL APPELLATE JURISDICTION: Civil Appeal No. 340 of 1957.

Appeal from the judgment and order dated November 29, 1954, of the Hyderabad High Court in Reference No. 234/5 of 1953-54.

K. N. Rajagopala Sastri, R. H. Dhebar and D. Gupta, for the appellant.

1959

The Commissioner
of Income-tax,
Hyderabad-Deccan

v.

Messrs. Vazir
Sultan & Sons

1959

*The Commissioner
of Income-tax,
Hyderabad-Deccan*

v.

*Messrs. Vazir
Sultan & Sons*

Bhagwati J.

A. V. Viswanatha Sastri, P. Rama Reddy and R. Mahalinga Iyer, for the respondents.

1959. March 20. The Judgment of Bhagwati and Sinha, JJ., was delivered by Bhagwati, J. Kapur, J., delivered a separate Judgment.

BHAGWATI, J.—This appeal with a certificate from the High Court of Judicature at Hyderabad raises the question whether the sum of Rs. 2,19,343 received by the assessee in the year of account relevant for the assessment year 1951-52 was a revenue receipt or a capital receipt.

The facts leading up to this appeal may be shortly stated :

The assessee is a registered firm consisting of five brothers and the wife of a deceased brother having equal shares in the profit and loss of the partnership. The firm was appointed the sole selling agents and sole distributors for the Hyderabad State for the cigarettes manufactured by M/s. Vazir Sultan Tobacco Co., Ltd., under the terms of a resolution of the Board of Directors dated January 6, 1931.

“ Mr. Baker reported that an arrangement had been come to for the time being whereby the firm of Vazir Sultan & Sons, were given the distributorship of “ Charminar ” Cigarettes within the H. E. H. the Nizam’s Dominions and that they were allowed a discount of 2% on the gross selling price.”

No written agreement was entered into between the Company and the assessee in respect of the above mentioned arrangement nor was there any correspondence exchanged between them in this behalf. In 1939 another arrangement was arrived at between the assessee and the company whereby the assessee was given a discount of 2% not only on the goods sold in the Hyderabad State but on all the goods sold in the Hyderabad State and outside Hyderabad State. It does not appear that the Board of Directors passed any resolution in support of this new arrangement nor was any agreement drawn up between the parties incorporating the said new arrangement.

On June 16, 1950, the Board of Directors passed the following resolution reverting to the old arrangement embodied in the resolution dated January 6, 1931 :—

“The Chairman, having referred to resolution No. 24 passed at the board meeting held on 6-1-31 and having reported that Vazir Sultan & Sons had agreed to revert to the arrangement outlined in that resolution with effect from 1-6-50, it was on the proposition of Mr. S. N. Bilgrami, seconded by Mr. N. B. Chenoy resolved that payment of the sum of O.S. Rs. 2,26,263 be made to Vazir Sultan & Sons by way of compensation, Vazir Sultan & Sons, to pay D. B. Akki & Co., out of that amount the sum of O. S. Rs. 6,920 also by way of compensation. Mr. Mohd. Sultan & Mr. Hameed Sultan stated that, as partners in the firm of Vazir Sultan & Sons, they did not take part in this resolution, although they had accepted on behalf of Vazir Sultan & Sons, the terms thereof.”

The sum of Rs. 2,19,343 was accordingly received by the assessee in the year of account 1359 F.

The Income-tax Officer included this sum in the assessee's total income and taxed it as a revenue receipt. On appeal the Appellate Assistant Commissioner held that the sum of Rs. 2,19,343 was not a revenue receipt but a capital receipt being compensation for the loss of the agency and as such not liable to tax. The Income-tax Officer (C Ward) Hyderabad thereupon preferred an appeal to the Income-tax Appellate Tribunal, Bombay, which held that the said sum received by the assessee was a revenue receipt and liable to tax. The assessee then applied to the Appellate Tribunal for a reference to the High Court under sec. 66(1) of the Income-tax Act and the Tribunal accordingly referred the following question of law to the High Court:—

“Whether the sum of O. S. Rs. 2,19,343 received by the assessee Firm from Vazir Sultan Tobacco Co., Ltd., is a revenue receipt or a capital receipt?”

The High Court answered the question in favour of the assessee stating the question in a different form, viz.,

1959

*The Commissioner
of Income-tax,
Hyderabad-Deccan*

v.

*Messrs. Vazir
Sultan & Sons*

Bhagwati J.

1959

*The Commissioner
of Income-tax,
Hyderabad-Deccan*

v.

*Messrs. Vazir
Sultan & Sons*

Bhagwati J.

“Whether the sum of O. S. Rs. 2,19,343 received by the assessee firm from Vazir Sultan Tobacco Co., Ltd., is liable to be taxed under the Indian Income-tax Act?”

The appellant thereafter applied to the High Court for a certificate of fitness which was granted by the High Court on February 21, 1955, and hence this appeal.

The question that falls to be determined is whether the sum which was in express terms of the resolution mentioned by way of “compensation” for the loss of the agency was a revenue receipt (trading receipt or an income receipt) as contended by the Revenue or a capital receipt as contended by the assessee.

It was urged on behalf of the appellant that the sole selling agency which was granted by the Company to the assessee in the year 1931 was merely expanded as regards territory in 1939 and what was done in 1951 was to revert to the old arrangement, and the structure or the profit-making apparatus of the assessee’s business was not affected thereby. The expansion as well as the restriction of the assessee’s territory were in the ordinary course of the assessee’s business and were mere accidents of the business which the assessee carried on and the sum of Rs. 2,19,343 received by the assessee as and by way of compensation for the restriction of the territory was a trading or an income receipt and was therefore liable to tax.

It was, on the other hand, contended on behalf of the assessee that it did not carry on business of acquiring and working agencies, that the agency acquired in 1931 was a capital asset of the assessee’s business of distributing Charminar cigarettes in the Hyderabad State, that the expansion of territory outside the Hyderabad State in 1939 was an accretion to the capital asset already acquired by the assessee, that the resolution of 1950 was in substance a termination or cancellation of the agency qua territory outside the Hyderabad State and resulted in the sterilisation of the capital asset qua that territory, that the sum of

Rs. 2,19,343 received by the assessee in the year of account was by way of compensation for the termination or cancellation of the agency outside Hyderabad State and being therefore compensation for the sterilisation *pro tanto* of a capital asset of the assessee's business was a capital receipt and was therefore not liable to tax.

The question whether a particular receipt is a revenue receipt or a capital receipt or a particular expenditure is a capital expenditure or a revenue expenditure is beset with considerable difficulty and one finds the Revenue and the assessee ranged on different sides taking up alternate contentions as it suits their purposes. As was observed by Lord Macmillan in *Van Den Berghs, Limited v. Clark* ⁽¹⁾ :—

“The reported cases fall into two categories, those in which the subject is found claiming that an item of receipt ought not to be included in computing his profits and those in which the subject is found claiming that an item of disbursement ought to be included among the admissible deductions in computing his profits. In the former case the Crown is found maintaining that the item is an item of income; in the latter, that it is a capital item. Consequently the argumentative position alternates according as it is an item of receipt or an item of disbursement that is in question, and the taxpayer and the Crown are found alternately arguing for the restriction or the expansion of the conception of income.”

The question has therefore to be dealt with irrespective of the one stand or the other which is taken by the Revenue or the assessee and the Court has got to determine what is the true character of the receipt or the expenditure.

In the case of the *Commissioner of Income-tax and Excess Profits Tax, Madras v. The South India Pictures Ltd., Karaikudi* ⁽²⁾ this Court endorsed the following statement of Lord Macmillan in *Van Den Berghs, Ltd. v. Clark* ⁽¹⁾ :

“That though in general the distinction between an income and a capital receipt was well recognised

1959

*The Commissioner
of Income tax,
Hyderabad-Deccan*
v.

*Messrs. Vazir
Sultan & Sons*

Bhagwati J.

(1) (1935) 19 Tax Cas. 390, 429.

(2) [1956] S.C.R. 223, 228.

1959

The Commissioner
of Income-tax,
Hyderabad-Deccan
v.

Messrs. Vazir
Sultan & Sons

Bhagwati J.

and easily applied, cases did arise where the item lay on the border line and the problem had to be solved on the particular facts of each case. No infallible criterion or test can be or has been laid down and the decided cases are only helpful in that they indicate the kind of consideration which may relevantly be borne in mind in approaching the problem. The character of the payment received may vary according to the circumstances. Thus the amount received as consideration for the sale of a plot of land may ordinarily be a capital receipt but if the business of the recipient is to buy and sell lands, it may well be his income."

While considering the case law it is necessary to bear in mind that the Indian Income-tax Act is not in *pari materia* with the British Income Tax statutes, it is less elaborate in many ways, subject to fewer refinements and in arrangement and language it differs greatly from the provisions with which the courts in England have had to deal. Little help can therefore be gained by attempting to construe the Indian Income-tax Act in the light of decisions bearing upon the meaning of the Income-tax legislation in England. But on analogous provisions, fundamental concepts and general principles unaffected by the specialities of the English Income-tax statutes, English authorities may be useful guides. (Vide the observations of the Privy Council in the *Commissioner of Income-tax v. Shaw Wallace & Co.* ⁽¹⁾; *Gopal Saran Narain Singh v. Commissioner of Income-tax* ⁽²⁾; *Commissioner of Income-tax, Bombay Presidency and Aden v. Chunnilal B. Mehta* ⁽³⁾ and *Raja Bahadur Kamakshya Narain Singh of Ramgarh v. C. I. T., Bihar & Orissa* ⁽⁴⁾).

Before embarking upon a discussion of the principles emerging from the various decisions bearing upon this question, it is necessary to advert to an argument which was addressed to us by the learned counsel for the appellant in connection with the Privy Council decision in the *Commissioner of Income-tax v. Shaw Wallace & Co.* ⁽¹⁾. That case was relied upon by the

(1) (1932) L.R. 59 I.A. 206, 212.

(2) (1935) L.R. 62 I.A. 207, 214.

(3) (1938) L.R. 65 I.A. 332, 349.

(4) (1943) L.R. 70 I.A. 180, 188.

Appellate Assistant Commissioner and the High Court as determinative of the question in favour of the assessee and it was strenuously urged before us on behalf of the Revenue that the authority of that decision was considerably shaken not only by the later Privy Council decision in *Raja Bahadur Kamakshya Narain Singh v. C. I. T., Bihar and Orissa* (1) but also by a decision of this Court in *Raghuvansi Mills Ltd. v. Commissioner of Income-tax, Bombay City* (2).

It may be remembered that the term "income" was understood by their Lordships of the Privy Council in *Shaw Wallace's Case* (3) to connote a periodical monetary return coming in with some sort of regularity or expected regularity from definite sources. The source may not necessarily be one which is expected to be continuously productive, but it must be one whose object is the production of a definite return excluding anything in the nature of a mere windfall. Income was thus likened pictorially to the fruit of a tree or the crop of a field (*Ibid* p. 212). This concept of "income" was adopted and in substance repeated by the Privy Council in *Gopal Saran Narain Singh's Case* (4) at p. 213, though Lord Russell of Killowen pronouncing the opinion of the Privy Council pithily remarked that anything which can properly be described as income is taxable under the Act unless properly exempted. The case of *Raja Bahadur Kamakshya Narain Singh* (1) struck a discordant note and Lord Wright delivering the opinion of the Board observed at p. 192 that it was not in their Lordships' opinion correct to regard as an essential element in any of these or like definitions a reference to the analogy of fruit or increase or sowing or reaping or periodical harvests and that such picturesque similes cannot be used to limit the true character of income in general. Lord Wright further observed at p. 194 :—

"Its applicability may in particular cases differ because the circumstances, though similar in some respects, may be different in others. Thus the profit realised on a sale of shares may be capital if the seller

1959

*The Commissioner
of Income-tax,
Hyderabad-Deccan*

v.

*Messrs. Vazir
Sultan & Sons*

Bhagwati J.

(1) (1943) L.R. 70 I.A. 180, 188.

(2) [1953] S.C.R. 177.

(3) (1932) L.R. 59 I.A. 206, 212.

(4) (1935) L.R. 62 I.A. 207, 214.

1959

The Commissioner
of Income-tax,
Hyderabad-Deccan
v.
Messrs. Vazir
Sultan & Sons
Bhagwati J.

is an ordinary investor changing his securities, but in some instances, at any rate, it may be income if the seller of the shares is an investment or an insurance company. Income is not necessarily the recurrent return from a definite source, though it is generally of that character. Income, again, may consist of a series of separate receipts, as it generally does in the case of professional earnings. The multiplicity of forms which "income" may assume is beyond enumeration. Generally, however, the mere fact that the income flows from some capital assets, of which the simplest illustration is the purchase of an annuity for a lump sum, does not prevent it from being income, though in some analogous cases the true view may be that the payments, though spread over a period, are not income, but instalments payable at specified future dates of a purchase price." (Vide *Secretary of State for India v. Scoble*)⁽¹⁾.

This Court in *Raghuvansi Mill's Case*⁽²⁾ also observed that the definition of "income" in *Shaw Wallace's Case*⁽³⁾ as a periodical monetary return coming in with some sort of regularity or expected regularity from definite sources must be read with reference to the particular facts of that case.

It was therefore urged on behalf of the Revenue that periodicity or recurring nature of the receipt was not a necessary ingredient of "income" nor was the existence of a material external source capable of producing a recurrent return necessary before a receipt could be treated as income chargeable to tax.

We are not unmindful of this criticism of the definition of "income" adopted by the Privy Council in *Shaw Wallace & Co.'s Case*⁽³⁾ and the concept of "income" may have to be thus revised. But even granting the proposition that is contended for by the Revenue the result is no different in the present case because the head of income under which the assessee before us has been assessed to Income-tax is "business" a definite source from which the income in question sought to be assessed is alleged to have been

(1) [1903] A.C. 299.

(2) [1953] S.C.R. 177.

(3) (1932) L.R. 59 I.A. 206, 212.

1959

—
*The Commissioner
of Income-tax,
Hyderabad-Deccan*
v.

*Messrs. Vazir
Sultan & Sons*

—
Bhagwati J.

derived and whether it is of a recurring or non-recurring nature therefore does not enter into the picture. The exemption from liability in regard to that income is claimed by the assessee, not on the ground of the applicability of s. 4(3)(vii) of the Income-tax Act but on the ground that it is not a revenue receipt but a capital receipt, being compensation paid by the Company to the assessee for the termination or cancellation of the agency qua territory outside Hyderabad State, a capital asset of the assessee's business.

What then are the considerations which have to be borne in mind in determining these vexed questions? The distinction between a capital expenditure and a revenue expenditure came up for consideration before this Court in *Assam Bengal Cement Co., Ltd. v. The Commissioner of Income-tax, West Bengal* ⁽¹⁾ and this Court laid down certain criteria for the determination as to whether a particular expenditure incurred by the assessee was a capital expenditure or a revenue expenditure. We need not therefore discuss that problem any further.

As to whether a particular receipt in the hands of an assessee is a capital receipt, or a revenue receipt, we had occasion to consider the same in the *Commissioner of Income-tax and Excess Profits Tax, Madras v. The South India Pictures Ltd., Karaikudi* ⁽²⁾. The assessee there carried on the business of distribution of films. In some instances the assessee used to produce or purchase films and then distribute the same for exhibition in different cinema halls and in other cases used to advance monies to producers of films produced with the help of monies so advanced. In the course of such business it advanced monies to the Jupiter Pictures for the production of these films and acquired the rights of distribution of the three films under three agreements in writing dated September, 1941, July 1942 and May 1943. In the accounting year ending March 31, 1946, and in the previous years the assessee had exploited its rights of distribution of the three pictures. On October 31, 1945, the

(1) [1955] 1 S.C.R. 972.

(2) [1956] S.C.R. 223, 228.

1959

The Commissioner
of Income-tax,
Hyderabad-Deccan

v.

Messrs. Vazir
Sultan & Sons

Bhagwati J.

assessee and the Jupiter Pictures entered into an agreement cancelling the three agreements relating to the distribution rights in respect of the three films and in consideration of such cancellation the assessee was paid Rs. 26,000 in all by the Jupiter Pictures as compensation. It was held by the Majority of this Court that the sum received by the assessee was a revenue receipt (and not a capital receipt) assessable under the Indian Income-tax Act inasmuch as:—

(1) the sum paid to the assessee was not truly compensation for not carrying on its business but was a sum paid in the ordinary course of business to adjust the relation between the assessee and the producers of the films;

(2) the agreements which were cancelled were by no means agreements on which the whole trade of the assessee had for all practical purposes been built and the payment received by the assessee was not for the loss of such a fundamental asset as was the ship managementship of the assessee in *Barr Crombie & Co., Ltd. v. Commissioners of Inland Revenue* ⁽¹⁾ and

(3) one could not say that the cancelled agreements constituted the framework or whole structure of the assessee's profit-making apparatus in the same sense as the agreement between the two margarine dealers in *Van Den Berghs Ltd. v. Clark* ⁽²⁾ was.

The criteria laid down by the majority judgment for determining whether the particular payment received by the assessee was income or was to be regarded as a capital receipt were:

(i) whether the agreements in question were entered into by the assessee in the course of carrying on its business of distribution of films, and

(ii) whether the termination of the agreements in question could be said to have been brought about in the ordinary course of business;

so that money received by the assessee as a result of or in connection with such termination of agreements could be regarded as having been received in the ordinary course of its business and therefore a trading receipt.

(1) (1945) 26 Tax Cas. 406.

(2) (1935) 19 Tax Cas. 390, 429.

A similar question arose in *Commissioner of Income-tax, Nagpur v. Rai Bahadur Jairam Valji*⁽¹⁾ where this Court followed the same line of reasoning. The question there related to a sum of Rs. 2,50,000 received by the assessee as damages or compensation for the premature termination of a contract dated May 9, 1940. The High Court on a reference under s. 66(1) of the Income-tax Act had held that the sum was a capital receipt in the hands of the assessee, and as such not liable to be taxed. It was contended on behalf of the Revenue that the contract dated May 9, 1940, was one entered into by the assessee in the ordinary course of his business, that the sum of Rs. 2,50,000 was paid admittedly as solatium for the cancellation of that contract, and that it was therefore a revenue receipt. The assessee on the other hand contended that the contract dated May 9, 1940, was for a period of 25 years of which more than 23 years had still to run at the time of the settlement, and it was therefore capital in character. Moreover, the true character of the agreement was that it brought into existence an arrangement which would enable him to carry on a business and was not itself any business and any payment made for the termination of such an agreement was a capital receipt.

This Court on the facts and circumstances of the case came to the conclusion that the contract in question was entered into by the assessee in the ordinary course of business and was one entered into in the carrying on of that business. The arrangement ultimately entered into between the parties in regard to the payment of the said sum of Rs. 2,50,000 was accordingly treated as an adjustment made in the ordinary course of business and the receipt was therefore held to be an amount paid as solatium for the cancellation of a contract entered into by a person in the ordinary course of business.

In the course of the discussion reference was made to agency agreements and this Court observed :—

“In an agency contract, the actual business consists in the dealings between the principal and his

1959

*The Commissioner
of Income-tax,
Hyderabad-Deccan*

v.

*Messrs. Vazir
Sultan & Sons*

Bhagwati J.

(1) [1959] Supp. 1 S.C.R. 110; 35 I.T.R. 148, 163.

1959

The Commissioner
of Income-tax,
Hyderabad-Deccan

v.

Messrs. Vazir
Sultan & Sons

—
Bhagwati J.

customers, and the work of the agent is only to bring about that business. In other words, what he does is not the business itself but something which is intimately and directly linked up with it. It is therefore possible to view the agency as the apparatus which leads to business rather than as the business itself on the analogy of the agreements in *Van Den Berghs Ltd. v. Clark* (1). Considered in this light, the agency right can be held to be of the nature of a capital asset invested in business. But this cannot be said of a contract entered into in the ordinary course of business. Such a contract is part of the business itself, not anything outside it as is the agency, and any receipt on account of such a contract can only be a trading receipt."

This Court further emphasised the distinction between an agency agreement and a contract made in the usual course of business and pointed out that the agreement could in any event be regarded as a capital asset of the agent which would be saleable. Such a concept would certainly be out of place with reference to a contract entered into in the course of business and any payment made for the non-performance or cancellation of such a contract could only be damages or compensation and could not, in law or fact, be regarded as an assignment of the rights under the contract. Once it was found that the contract was entered into in the ordinary course of business, any compensation received for its termination would be a revenue receipt, irrespective of whether its performance was to consist of a single act or a series of acts spread over a period.

While thus indicating that an agency could be treated as a capital asset of the business this Court guarded itself against its being understood as deciding that the compensation paid for cancellation of an agency contract must always and as a matter of law be held to be a capital receipt and it made the following pertinent observations:—

"Such a conclusion will be directly opposed to the decision in *Kelsall's case* (2) and the *Commissioner*

(1) [1935] 19 Tax Cas. 390, 429.

(2) (1938) 21 Tax Cas. 608.

of *Income-tax and Excess Profits Tax, Madras v. The South India Pictures Ltd., Karaikudi* (1). The fact is that an agency contract which has the character of a capital asset in the hands of one person may assume the character of a trading receipt in the hands of another, as for example, when the agent is found to make a trade of acquiring agencies and dealing with them. The principle was thus stated by Romer, L. J., in *Golden Horse Shoe (New) Ltd. v. Thurgood* (2) :

‘The determining factor must be the nature of the trade in which the asset is employed. The land upon which a manufacturer carries on his business is part of his fixed capital. The land with which a dealer in real estate carries on his business is part of his circulating capital. The machinery with which a manufacturer makes the articles that he sells is part of his fixed capital. The machinery that a dealer in machinery buys and sells is part of his circulating capital, as is the coal that a coal merchant buys and sells in the course of his trade. So, too, is the coal that a manufacturer of gas buys and from which he extracts his gas.’ Therefore when a question arises whether a payment of compensation for termination of an agency is a capital or a revenue receipt, it would have to be considered whether the agency was in the nature of capital asset in the hands of the assessee, or whether it was only part of his stock-in-trade. Thus in *Barr Crombie & Sons Ltd. v. Commissioners of Inland Revenue* (3), the agency was found to be practically the sole business of the assessee, and the receipt of compensation on account of it was accordingly held to be a capital receipt, while in *Kelsall’s case* the agency which was terminated was one of several agencies held by the assessee and the compensation amount received therefor was held to be a revenue receipt, and that was also the case in the *Commissioner of Income-tax and Excess Profits Tax, Madras v. The South India Pictures Ltd., Karaikudi* (1).”

We may in this context also note the further observations made by this Court :—

(1) [1956] S.C.R. 223 228.

(2) (1933) 18 Tax Cas. 280, 300.

(3) (1945) 26 Tax Cas. 406.

1959

—
The Commissioner
of Income-tax,
Hyderabad-Deccan
v.
Messrs. Vazir
Sultan & Sons
—
Bhagwati J.

1959

*The Commissioner
of Income-tax,
Hyderabad-Deccan*

v.

*Messrs. Vazir
Sultan & Sons*

Bhagwati J.

“But apart from these and similar instances, it might, in general, be stated that payments made in settlement of rights under a trading contract are trading receipts and are assessable to revenue. But where a person who is carrying on business is prevented from doing so by an external authority in the exercise of a paramount power and is awarded compensation therefor, whether that receipt is a capital receipt or a revenue receipt will depend upon whether it is compensation for injury inflicted on a capital asset or on a stock-in-trade. The decision in the *Glenboig Union Fireclay Co., Ltd. v. The Commissioners of Inland Revenue* ⁽¹⁾ applies to this category of cases. There, the assessee was carrying on business in the manufacture of fire-clay goods and had, for the performance of that business, acquired a fire clay field on lease. The Caledonian Railway which passed over the field prohibited the assessee from excavating the field within a certain distance of the rails, and paid compensation therefor in accordance with the provisions of a statute. It was held by the House of Lords that this was a capital receipt and was not taxable on the ground that the compensation was really the price paid “for sterilising the asset from which otherwise profit might have been obtained.” That is to say, the fire clay field was a capital asset which was to be utilised for the carrying on of the business of manufacturing fire clay goods and when the assessee was prohibited from exploiting the field, it was an injury inflicted on his capital asset. Where, however, the compensation is referable to injury inflicted on the stock-in-trade, it would be a revenue receipt. (Vide the *Commissioners of Inland Revenue v. Newcastle Breweries Ltd.* ⁽²⁾.”

It is no doubt true that this Court was not concerned with any agency agreement in the last mentioned case and the observations made by this Court there were by way of obiter dicta. The obiter dicta of this Court, however, are entitled to considerable weight and we on our part fully endorse the same. The earlier case of *Commissioner of Income-tax and Excess Profits Tax*,

(1) (1922) 12 Tax Cas. 427.

(2) (1927) 12 Tax Cas. 927.

Madras v. The South India Pictures Ltd. ⁽¹⁾ was indeed a case where the assessee had entered into agency agreements for the exploitation of the three films in question, but in that case the conclusion was reached that entering into such agency agreements for acquiring the films was a part of the assessee's business and the agreements in question having been entered into by the assessee in the ordinary course of business the cancellation of those agreements was also a part of the assessee's business and was resorted to in order to adjust the relation between the assessee and the producer of those films.

It would not be profitable to review the various English decisions bearing on this question as they have been exhaustively reviewed in the above decisions of this Court. The position as it emerges on a consideration of these authorities may now be summarised. The first question to consider would be whether the agency agreement in question for cancellation of which the payment was received by the assessee was a capital asset of the assessee's business, constituted its profit making apparatus and was in the nature of its fixed capital or was a trading asset or circulating capital or stock-in-trade of his business. If it was the former the payment received would be undoubtedly a capital receipt; if, however, the same was entered into by the assessee in the ordinary course of business and for the purpose of carrying on that business, it would fall into the latter category and the compensation or payment received for its cancellation would merely be an adjustment made in the ordinary course of business of the relation between the parties and would constitute a trading or a revenue receipt and not a capital receipt.

We may perhaps appropriately refer at this stage to an aspect of this question which was canvassed before us with some force and it was that there was no enforceable agreement as between the assessee and the Company which could be made the subject-matter of a legal claim for damages or compensation at his instance in the event of its termination or cancellation by the Company. The agency agreement was

1959

*The Commissioner
of Income-tax,
Hyderabad-Deccan*

v.

*Messrs. Vazir
Sultan & Sons*

Bhagwati J.

(1) [1956] S.C.R. 223, 228.

1959

*The Commissioner
of Income-tax,
Hyderabad-Deccan*
v.
*Messrs. Vazir
Sultan & Sons*
Bhagwati J.

terminable at the will of the Company and if the Company chose to do so the assessee had no remedy at law in regard to the same. It is, however, to be remembered that in all these cases one has really got to look to the nature of the receipt in the hands of the assessee irrespective of any consideration as to what was actuating the mind of the other party. As Rowlatt, J., observed in the case of *Chibbett v. Joseph Robinson & Sons* (1):—

“As Sir Richard Henn Collins said, you must not look at the point of view of the person who pays and see whether he is compellable to pay or not; you have to look at the point of view of the person who receives, to see whether he receives it in respect of his services, if it is a question of an office and in respect of his trade, if it is a question of trade and so on. You have to look at his point of view to see whether he receives it in respect of those considerations. This is perfectly true. But when you look at that question from what is described as the point of view of the recipient, that sends you back again, looking, for that purpose, to the point of view of the payer; not from the point of view of compellability or liability, but from the point of view of a person inquiring what is this payment for; and you have to see whether the maker of the payment makes it for the services and the receiver receives it for the services.”

The learned Judge further observed at p. 61:—

“But at any rate it does seem to me that compensation for loss of an employment which need not continue, but which was likely to continue, is not an annual profit within the scope of the Income-tax at all.” (See also *W. A. Guff v. Commissioner of Income-tax, Bombay City*) (2) where the question whether the amount paid was compensation for which the employer was liable or was a payment made ex-gratia was considered immaterial for the purpose of the decision in that case).

It was also urged that the agency in question before us was not an enduring asset of the assessee's business as in its very nature it was terminable at will,

(1) (1924) 9 Tax Cas. 48, 60.

(2) [1957] 31 I.T.R. 826.

there being no agreement or arrangement for a fixed term between the assessee and the Company. On the analogy of the test laid down by this Court in *Assam Bengal Cement Co., Ltd. v. The Commissioner of Income-tax, West Bengal* ⁽¹⁾ while considering the distinction between a capital expenditure and a revenue expenditure, it was argued that the agency agreement in question could not be a capital asset of the assessee's business in so far as it was not of an enduring character and the compensation paid for its termination could not therefore be a capital receipt in the hands of the assessee. Whatever be the position, however, in the case of the acquisition of an asset by the assessee by making a disbursement for the purchase of the same, similar considerations would not necessarily operate when the amount is received by the assessee for the termination or cancellation of an asset of his business. The character of such a receipt would indeed have to be determined having regard to the fact whether the asset in question was a capital asset of the business or a trading asset thereof. For this purpose it will be immaterial whether that asset was of an enduring character or was one which was terminable at will.

We have therefore got to determine whether the agency in question before us was a capital asset of the assessee's business. One of the relevant considerations in the matter of such determination has been whether the asset was in the nature of fixed capital or constituted the circulating capital or stock-in-trade of the assessee's business. This question was thus dealt with by Viscount Haldane in *John Smith & Sons v. Moore* ⁽²⁾ :—

“But what was the nature of what the Appellant here had to deal with? He had bought as part of the capital of the business his father's contracts. These enabled him to purchase coal from the colliery owners at what we were told was a very advantageous price, about fourteen shillings per ton. He was able to buy at this price because the right to do so was part of the

1959

The Commissioner
of Income-tax,
Hyderabad-Deccan
v.

Messrs. Vazir
Sultan & Sons

Bhagwati J.

(1) [1955] 1 S.C.R. 972.

(2) (1921) 12 Tax Cas. 266, 282.

1959

*The Commissioner
of Income-tax,
Hyderabad-Deccan*

v.

*Messrs. Vazir
Sultan & Sons*

Bhagwati J.

assets of the business. Was it circulating capital? My Lords, it is not necessary to draw an exact line of demarcation between fixed and circulating capital. Since Adam Smith drew the distinction in the Second Book of his "Wealth of Nations", which appears in the chapter on the Division of Stock, a distinction which has since become classical, economists have never been able to define much more precisely what the line of demarcation is. Adam Smith described fixed capital as what the owner turns to profit by keeping it in his own possession, circulating capital as what he makes profit of by parting with it and letting it change masters. The latter capital circulates in this sense. My Lords, in the case before us the Appellant, of course, made profit with circulating capital, by buying coal under the contracts he had acquired from his father's estate at the stipulated price of fourteen shillings and reselling it for more, but he was able to do this simply because he had acquired, among other assets of his business, including the goodwill, the contracts in question. It was not by selling these contracts, of limited duration though they were, it was not by parting with them to other masters, but by retaining them, that he was able to employ his circulating capital in buying under them. I am accordingly of opinion that though they may have been of short duration, they were none the less part of his fixed capital".

In the case before us the agency agreement in respect of territory outside the Hyderabad State was as much an asset of the assessee's business as the agency agreement within the Hyderabad State and though expansion of the territory of the agency in 1939 and the restriction thereof in 1950 could very well be treated as grant of additional territory in 1939 and the withdrawal thereof in 1950, both these agency agreements constituted but one employment of the assessee as the sole selling agents of the Company. There is nothing on the record to show that the acquisition of such agencies constituted the assessee's business or that these agency agreements were entered into by the assessee in the carrying on of any such business.

The agency agreements in fact formed a capital asset of the assessee's business worked or exploited by the assessee by entering into contracts for the sale of the "charminar" cigarettes manufactured by the Company to the various customers and dealers in the respective territories. This asset really formed part of the fixed capital of the assessee's business. It did not constitute the business of the assessee but was the means by which the assessee entered into the business transactions by way of distributing those cigarettes within the respective territories. It really formed the profit-making apparatus of the assessee's business of distribution of the cigarettes manufactured by the Company. If it was thus neither circulating capital nor stock-in-trade of the business carried on by the assessee it could certainly not be anything but a capital asset of its business and any payment made by the Company as and by way of compensation for terminating or cancelling the same would only be a capital receipt in the hands of the assessee.

It would not make the slightest difference for this purpose whether either one or both of the agency agreements were terminated or cancelled by the Company. The position would be the same in either event. As was observed by Lord Wrenbury in the *Glenboig Union Fire-Clay Co., Ltd. v. The Commissioners of Inland Revenue* (1) at p. 465 :—

"The matter may be regarded from another point of view ; the right to work the area in which the working was to be abandoned was part of the capital asset consisting of the right to work the whole area demised. Had the abandonment extended to the whole area all subsequent profit by working would, of course have been impossible but it would be impossible to contend that the compensation would be other than capital. It was the price paid for sterilising the asset from which otherwise profit might have been obtained. *What is true of the whole must be equally true of part.*"

If both the agency agreements, viz., one for the territory within the Hyderabad State and the other for the territory outside Hyderabad State had been

1959

*The Commissioner
of Income-tax,
Hyderabad-Deccan*

v.

*Messrs. Vazir
Sultan & Sons*

Bhagwati J.

(1) (1922) 12 Tax Cas. 427.

1959

The Commissioner
of Income-tax,
Hyderabad-Deccan

v.

Messrs. Vazir
Sultan & Sons

Bhagwati J.

terminated or cancelled on payment of compensation, the whole profit-making structure of the assessee's business would have been destroyed. Even if one of these agency agreements was thus terminated, it would result in the destruction of the profit-making apparatus or sterilisation of the capital asset *pro tanto* and if in the former case the receipt in the hands of the assessee would only be a capital receipt, equally would it be a capital receipt if compensation was obtained by the assessee for the termination or cancellation of one of these agency agreements which formed a capital asset of the assessee's business.

The facts of the present case are closely similar to those which obtained in the *Commissioner of Income-tax v. Shaw Wallace & Co.* (1). In that case also the assessees had for a number of years prior to 1928 acted as distributing agents in India of the Burma Oil Company, and the Anglo-Persian Oil Company, but had no formal agreement with either Company. In or about the year 1927 the two companies combined and decided to make other arrangements for the distribution of their products. The assessee's agency of the Burma Company was accordingly terminated on December 31, 1927, and that of the Anglo-Persian Company on June 30, following. Some time in the early part of 1928 the Burma Company paid to the assessee a sum of Rs. 12,00,000 "as full compensation for cessation of the agency" and in August of the same year the Anglo-Persian Company paid them another sum of Rs. 3,25,000 as "compensation for the loss of your office as agents to the company". On the facts and circumstances of the case the Privy Council came to the conclusion that the sums could only be taxable if they were the produce, or the result of, carrying on the agencies of the oil companies in the year in which they were received by the assessees. But when once it was admitted that they were sums received, not for carrying on that business, but as some sort of solatium for its compulsory cessation, the answer seemed fairly plain. Whatever be the criticism in regard to the concept of income adopted in this case noted

(1) (1932) L.R. 59 I.A. 206, 212.

earlier in this judgment, the decision could just as well be supported on the grounds which we have hereinbefore discussed and was quite correct, the payments having been received by the assessees as and by way of compensation for the termination or cancellation of the agency agreements in question which were in fact the capital assets of the assessee's business.

The Appellate Assistant Commissioner as well as the High Court were thus justified in the conclusion to which they came, viz., that the sum of Rs. 2,19,343 received by the assessee from the Company was a capital receipt.

The result, therefore, is that the appeal fails and will stand dismissed with costs throughout.

KAPUR, J.—I have had the advantage of perusing the judgment prepared by my learned brother Bhagwati, J., but with great respect I am unable to agree and my reasons are these.

The sole question for determination in this case is as to whether a sum of Rs. 2,26,263 received by the assessees from Vazir Sultan Tobacco Co. Ltd. as compensation for the termination of their agency for the distribution of 'charminar' cigarettes in areas of India other than Hyderabad State is or is not taxable in the hands of the assessees. The answer to this question depends on whether the amount has been received by the assessees as a capital or a revenue receipt. In 1931 the assessees were appointed distributing agents for Hyderabad State only and for the rest of India in 1939, the agency commission in each case being a discount of 2% on the gross selling price. The agency of 1939 was terminated by a resolution dated June 16, 1950, on payment of the compensation amount already mentioned but the assessees continued to be distributors for Hyderabad State. It must here be mentioned that the agency in question was terminable at will, and that any compensation paid for it would prima facie be revenue.

During the accounting year the amount of income, profits and gains of the assessees from the cigarette distribution business and from another source, i. e.,

1959

*The Commissioner
of Income-tax,
Hyderabad-Deccan*

v.

*Messrs. Vazir
Sultan & Sons*

Bhagwati J.

Kapur J.

1959

The Commissioner
of Income-tax,
Hyderabad-Deccan

v.

Messrs. Vazir
Sultan & Sons

Kapur J.

Acid Factory within the State of Hyderabad was Rs. 4,53,159. The order of the Income-tax Officer or the Appellate Tribunal does not show how much of this sum was attributable to the Cigarette distribution business and how much to the other source. There is no finding as to how and to what extent, if any, the business of the assesseees was affected by the cesser of distribution business outside that State.

The question now arises did the assesseees receive the compensation in lieu of the commission they otherwise might or would have earned if the agreement had continued or did they receive it as compensation for the destruction of a profit-making asset. The answer to this question would again be dependent upon whether the receipt in question is attributable to a fixed capital asset or to circulating capital. These two terms have been used in a number of cases but as applied to agencies compensation will be a capital receipt if it is received as the value of the agency, i.e., it is a price of the business as if it is brought to sale. On the other hand it is revenue receipt if it is paid in lieu of profits or commission. In *Van Den Berghs Ltd. v. Clark* ⁽¹⁾ Lord Macmillan described circulating capital as "capital which is turned over and in the process of being turned over yields profit or loss. Fixed capital is not involved directly in that process and remains unaffected by it". As was said by Lord Macmillan in the same case, it is not possible to lay down any single test as infallible or any single criterion as decisive in the determination of the question. Ultimately it must depend upon the facts of a particular case.

The assesseees rested their case on the decision of the Privy Council in *Commissioner of Income-tax v. Shaw Wallace & Co.* ⁽²⁾ on which the High Court has mainly relied. In that case the assesseees carried on business in India as merchants and agents for various companies. They were distributing agents for two oil companies. These two agencies were terminated and a sum of Rs. 12,00,000 was paid as compensation for the loss of these agency rights and the question was

(1) (1935) 19 Tax Cas. 390.

(2) (1932) L.R. 59 I.A. 206.

whether this was a capital payment. It was held to be a capital and not a revenue receipt because the sum received was not the result of carrying on the agencies of the oil companies, in other words, it could not be regarded as profits or gains from carrying on the business but was received in the nature of a solatium for cessation. The case was decided on the interpretation of the word 'business' as defined in s. 2(4) of the Income-tax Act, under which it "includes any trade, commerce or manufacture, or any adventure or concern in the nature of trade, commerce or manufacture". These words, it was held, were wide "but underlying each of them is the fundamental idea of the continuous exercise of an activity which was also the idea underlying the relevant words of s. 10(1) of the Act, "in respect of the profits or gains of any business carried on by him", i. e., it is to be the profit earned by a process of production. The test of income was its periodicity because it connotes a periodical monetary return. This test of periodicity was not accepted by the Privy Council itself in *Raja Bahadur Kamakshya Narain Singh's case* (1). Lord Wright there said "income is not necessarily the recurrent return from a definite source, though it is generally so". The test of periodicity was rejected by this Court in *Raghuvanshi Mills Ltd. v. Commissioner of Income-tax* (2) where Bose, J., said that the remarks of periodical monetary return must be confined to the facts of that case and it was held that money received from an insurance company for insurance against losses was income representing loss of profits as opposed to loss of capital. In a later case *The Commissioner of Income-tax v. The South India Pictures Ltd.* (3) it was said that if Shaw-Wallace & Co. had other agencies similar to those of the two oil companies it would be difficult to reconcile the decision in that case with the later decisions in *Kelsall Parsons & Co. v. Commissioners of Inland Revenue* (4) and other cases (Per Das, C. J.). In view of the decision in the *South India Pictures' case* and the observations of Bose, J., in the

1959

*The Commissioner
of Income-tax,
Hyderabad-Deccan*
v.
*Messrs. Vazir
Sultan & Sons*
Kapur J.

(1) (1943) L.R. 70 I.A. 180.

(2) [1953] S.C.R. 177, 183.

(3) [1956] S.C.R. 223, 232.

(4) (1938) 21 Tax Cas. 608.

1959
 —
 The Commissioner
 of Income-tax,
 Hyderabad-Deccan
 v.
 Messrs. Vazir
 Sultan & Sons
 —
 Kapur J.

case of *Raghuvanshi Mills Ltd.* (1) the authority of *Shaw Wallace & Co.'s* case (2) must be taken to be considerably shaken. We have then to see how the question has to be determined.

Various tests have been laid down in decided cases. According to Lord Cave, L. C., an expenditure made not only once and for all but with a view to bringing into existence an asset or an advantage for the enduring benefit of a trade has been treated as properly attributable to capital and not to revenue. (*British Insulated Cables* (3)). According to Lord Atkinson the word "asset" need not be confined to "something material" and Romer, L. J., has added that the advantage paid for need not be "of a positive character" and may consist in the getting rid of an item of fixed capital that is of an onerous character (*Anglo-Persian Oil Co. v. Dale* (4)). If the receipt represents the aggregate of profits which an assessee would otherwise have received over a series of years the lump sum might be regarded as of the same nature as the ingredients of which it was composed (19 Tax Cas. 390 at p. 431) (5) but it is not necessarily in itself an item of income (per Lord Buckmaster in *Glenboig Union Fireclay Co.* (6)).

In *Van Den Berghs' case* (7) there were three agreements between a British and a Dutch company operative till 1940 making it possible for them to carry on their business 'in friendly alliance' and providing for the sharing of profits in certain proportions. The agreements were terminated in 1927 and the Dutch company paid the English company a sum of £ 450,000 as compensation. The question was the character of the receipt—whether capital or revenue. It was held by the House of Lords that it was the former because the agreements were not "ordinary commercial contracts in the course of carrying on their trade; they were not contracts for the disposal of their employees or for the engagement of agents or other employees

(1) [1953] S.C.R. 177, 183.

(2) (1932) L.R. 59 I.A. 206.

(3) [1926] A.C. 205, 213, 222.

(4) [1932] 1 K. B. 124, 146.

(5) *Van Den Berghs Ltd. v. Clark.*

(6) (1922) 12 Tax Cas. 427, 464.

(7) (1935) 19 Tax Cas. 390.

for the conduct of their business nor were they merely agreements as to how their trading profits when earned should be distributed as between the contracting parties. On the contrary the agreements related to the whole structure of the recipient's profit making apparatus. They regulated its activities, defined what it might or it might not do and affected the whole conduct of its business". According to Lord Macmillan if the agreements formed the fixed framework within which the circulating capital operated, then they are not incidental to the working of its profit-making machine but were essential parts of the mechanism itself and therefore they would result in a capital receipt and not revenue receipt. Thus the agreements were designed to ensure that the business was carried on to the best advantage but they did not themselves form part of the business. They were not agreements which must be regarded as pertinent to trading activities which yielded profits. As such the totality of payments on account of those agreements were held to be a capital receipt.

The various decided cases demarcate the areas on the two sides of the line in which a receipt may lie and in every case it has to be determined as to whether it falls on one side or the other. The simplest case is of income from property or business as distinct from something received in lieu of property or business itself. One illustration of this is insurance against fire, destruction or damage and insurance against loss of profit, the former would bring in compensation in the nature of a capital. Another instance is where the whole business is bought over and the receipt is the price of the business itself as opposed to a lump sum payment for the loss of profit calculated on a proper basis. The test of income, i. e., periodicity or recurrence at fixed intervals has been doubted in this Court. *Raghuvanshi Mills* (1).

Another test is afforded by cases of tangible immovable property. If an owner of such property is paid compensation for not working a part of his property,

(1) [1953] S.C.R. 177, 183.

1959

*The Commissioner
of Income-tax,
Hyderabad-Deccan*

v.

*Messrs. Vazir
Sultan & Sons*

Bhagwati J.

1959

The Commissioner
of Income-tax,
Hyderabad-Deccan

v.

Messrs. Vazir
Sultan & Sons

Bhagwati J.

e. g., a part of the demised premises the compensation is not profit because it is payment for sterilising that part of the asset from which otherwise profit might have been obtained. (*Glenboig Union Fireclay case* ⁽¹⁾ at p. 464). There is no difference in cases of this kind whether the abandonment extends to the whole area or is circumscribed to a part because in either case it is sterilising an asset from which otherwise profit might have been obtained. "It makes no difference whether it may be regarded as a sale of the asset out and out or it be treated merely as a means of preventing the acquisition of profit that would otherwise be gained. In either case the asset of the company to that extent has been sterilised or destroyed".

Another test is whether the agreement related to the whole structure of recipient's profit-making apparatus and affected the whole conduct of his business or was the loss of a part of the fixed framework of the business. If it is, it is capital (*Van Den Bergh's case* ⁽²⁾). But compensation for temporary and variable elements of the recipient's profit-making apparatus would be revenue (*MacDonald's case* ⁽³⁾). If the agreement affects the whole structure and character of the recipient's business then it is capital but not if the structure of the business is so designed as to absorb the shocks as by the cancellation of one agency (*Kelsall Parson's case* ⁽⁴⁾). In *Bush Beach and Gent Ltd. v. Road* ⁽⁵⁾ again the test of how the cancellation of the agreement affected the recipient's business was applied. *Barr Crombie's case* ⁽⁶⁾ is a case of capital asset as there the recipient lost his entire business which resulted in reduction of staff, salaries and even in office accommodation. The result was the cesser of its trading existence. The transaction took the form of a transfer for a price from one party to another of something that formed part of the enduring asset of one of them. Compensation for the loss of an agency would be for the loss of a capital asset if the termination of the

(1) (1922) 12 Tax Cas. 427, 464.

(2) (1935) 19 Tax Cas. 390.

(3) (1955) 36 Tax Cas. 388.

(4) (1938) 21 Tax Cas. 608.

(5) (1939) 22 Tax Cas. 519.

(6) (1945) 26 Tax Cas. 406.

agency was a damage to the recipient's business structure such as to destroy or materially cripple the whole structure involving serious dislocation of the normal commercial organisation but if it was merely compensation for the loss of trading profit, i. e., in respect of commissions or it took the place of commission that would have been earned if the engagement had continued then it is revenue (*Wiseburg v. Domville*)⁽¹⁾. So that the decision as to whether compensation was capital or revenue would depend upon whether the cessation of the agency destroys or materially cripples the whole structure of the recipient's profit making apparatus or whether the loss is of the whole or part of the framework of business.

If we apply these tests to the agreement which has been terminated in the present case, it does not fall in any of the class of cases of destruction of a capital asset.

For the appellant reliance was placed on the observations of Venkatarama Aiyar, J., in *Commissioner of Income-tax v. Rai Bahadur Jairam Valji*⁽²⁾ where it was pointed out that in an agency contract the actual business consists in the dealings between the principal and his customers and the work of the agent is only to bring about that business. In other words what the agent does is not business itself but something which is intimately and directly linked with it. But an examination of the context shows that that is not what these observations mean. The point that was to be decided in that case was whether a payment of compensation for the cancellation of a trading contract was a capital or revenue receipt, and dealing with decisions relating to the cancellation of agency contracts which were quoted in support of the contention that they were capital, the learned Judges observed that considerations applicable to agency contracts were inapplicable to trading contracts, because the two classes of contracts, were essentially different, and these differences were there pointed out. The purpose of these observations was to show that receipts from

1959

*The Commissioner
of Income-tax,
Hyderabad-Deccan*
v.
*Messrs. Vazir
Sultan & Sons*
Bhagwati J.

(1) [1956] 36 Tax Cas. 527.

(2) [1959] Supp. 1 S.C.R. 110; [1959] 35 I.T.R. 148, 161, 163.

1959

The Commissioner
of Income-tax,
Hyderabad-Deccan

v.

Messrs. Vazir
Sultan & Sons

—
Bhagwati J.

trading contracts were revenue and not that receipts from agency contracts are capital. That that is the true scope of these observations is clear from the following passage :

“In holding that compensation paid on the cancellation of a trading contract differs in character from compensation paid for cancellation of an agency contract, we should not be understood as deciding that the latter must always, and as a matter of law be held to be a capital receipt. Such a conclusion will be directly opposed to the decisions in *Kelsall's case* ⁽¹⁾ and *Commissioner of Income-tax v. South India Pictures Ltd* ⁽²⁾. The fact is that an agency contract which has the character of a capital asset in the hands of one person may assume the character of a trading receipt in the hands of another, as, for example, when the agent is found to make a trade of acquiring agencies and dealing with them”.

The Court there observed that when the assessee holds a number of agencies, the compensation paid for cancellation of any of them could be regarded as revenue receipt. This is inconsistent with the conclusion that an agency contract must always be regarded as a capital asset. The learned Judges further observed that they were not elaborating this part as they were there concerned with a trading contract and therefore the statement as to when receipts from agency contracts could be regarded as revenue receipts cannot be read as exhausting the circumstances under which they could be held to be revenue.

As a matter of fact there are three kinds of cases of agencies shown by the decided cases : (1) *Kelsall Parsons' case* ⁽¹⁾ where the recipient was carrying on several agencies and the test laid down was whether the business structure could absorb a shock of the termination of one. (2) The other is where the compensation is for a temporary and variable element of assessee's profit making apparatus ; *MacDonald's case* ⁽³⁾. (3) The third class of cases is represented by

(1) (1938) 21 Tax Cas. 608.

(2) [1956] S.C.R. 223, 232.

(3) (1955) 36 Tax Cas. 388.

Fleming & Co.'s case⁽¹⁾ where the rights and advantages surrendered were such as to destroy or materially cripple the whole structure of the profit making apparatus.

The agencies themselves are of different kinds: (1) where the agent himself carries on the business and sells the product of the principal and gets commission for it; (2) where the agent's function is confined to bringing the principal and the customer together and he gets agency commission for the performance of only that service; (3) where the agent is a distributor and distributes the products of the principal through his sub-agents and charges commission for the distribution work. Cases (1) and (3) would not strictly fall within the scope of the observations in *Commissioner of Income-tax v. R. B. Jairam Valji*⁽²⁾ and case (2) would fall within the second class of agreements mentioned in *Van Den Bergh's case*⁽³⁾.

The agreement which is now before us and which was surrendered was terminable at will. The amount of profit which the assessee made from working the agency contract in Hyderabad State alone was much more than the amount which the assessee received for the termination of the whole of their agency outside the State. Thus it is clear that the termination did not affect the trading activities of the assessee and therefore the termination of the contract viewed against the background of the assessee's business organisation and profit-making structure appears to be no more than compensation for the loss of future profit and commission. The true effect of the facts of this case appears to be this that in 1939 the assessee's area of distribution was increased from the State of Hyderabad to the whole of India and in 1950 it was again reduced to the original area of 1931. The assessee never lost their agency. As a result of this contraction of area they at the most have lost some agency commission. The compensation therefore was in the nature of surrogatum and in this view of the matter it is revenue and not capital.

(1) (1951) 33 Tax Cas. 57.

(2) [1959] Supp. 1 S.C.R. 110; [1959] 35 I.T.R. 148, 161, 163.

(3) (1935) 19 Tax Cas. 390.

1959

*The Commissioner
of Income-tax,
Hyderabad-Deccan*

v.

*Messrs. Vazir
Sultan & Sons*

Bhagwati J.

1959

*The Commissioner
of Income-tax,
Hyderabad-Deccan*

v.

*Messrs. Vazir
Sultan & Sons*

Bhagwati J.

I would therefore allow this appeal with costs throughout.

BY COURT: In accordance with the majority judgment of the Court, the appeal is dismissed with costs throughout.

Appeal dismissed.

1959

March 26.

GHERULAL PAKKH

v.

MAHADEODAS MAIYA AND OTHERS

(JAFER IMAM, A. K. SARKAR and
K. SUBBA RAO, JJ.)

Wager—Collateral contract—Agreement of partnership to enter into wagering transactions—Legality—Indian Contract Act, 1872 (9 of 1872), ss. 23, 30.

The question for determination in this appeal was whether an agreement of partnership with the object of entering into wagering transactions was illegal within the meaning of s. 23 of the Indian Contract Act. The appellant and the respondent No. 1 entered into a partnership with the object of entering into forward contracts for the purchase and sale of wheat with two other firms and the agreement between them was that the respondent would enter into the contracts on behalf of the partnership and the profit or loss would be shared by the parties equally. The transactions resulted in loss and the respondent paid the entire amount due to the third parties. On the appellant denying his liability for the half of the loss, the respondent sued him for the recovery of the same and his defence, inter alia, was that the agreement to enter into the wagering contracts was unlawful under s. 23 of the Contract Act. The trial Court dismissed the suit. The High Court on appeal held that though the wagering contracts were void under s. 30 of the Indian Contract Act, the object of the partnership was not unlawful within the meaning of the Act and decreed the suit. It was contended on behalf of the appellant (1) that a wagering contract being void under s. 30 of the Contract Act, was also forbidden by law within the